Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Annual Assessment of the Status of	)	MB Docket No. 05-255
Competition in the Market for the	)	
Delivery of Video Programming	)	

NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION
INITIAL COMMENTS

NATIONAL TELECOMMUNICATIONS
COOPERATIVE ASSOCIATION

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INITIAL COMMENTS

The National Telecommunications Cooperative Association (NTCA) hereby submits these comments in response to the Federal Communications Commission's (Commission's or FCC's) Notice of Inquiry in the above referenced matter.[1] In its NOI, the Commission solicits data and information on the status of competition in the market for the delivery of video programming for its twelfth annual report to Congress on the status of competition in the market for the delivery of video programming. In these Comments, NTCA provides information about and insight into the challenges of small companies providing video services in rural America.

I. INTRODUCTION AND SUMMARY

NTCA is an industry association representing rural telecommunications providers. Established in 1954 by eight rural telephone cooperatives, today NTCA represents more than 560 rural rate-of-return regulated telecommunications providers. All of NTCA's members are full service incumbent local exchange carriers and many of its members provide wireless, Internet,

[1] In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, Notice of Inquiry, MB Docket No. 05-255 (rel. Aug. 12, 2005)(NOI).

video and long distance service to their communities. More than half of NTCA's members are multi-channel video programming distributors (MVPDs).[2]

Most NTCA members who provide video service to their communities do so according to traditional CATV coaxial, fiber cable, or Direct Broadcast Satellite (DBS). However, more and more of NTCA's members are utilizing the so-called Telco-TV model, providing video service via alternative broadband infrastructures and technologies, such as Digital Subscriber Line (DSL) over copper facilities.[3] These companies serve the most rural segments of this country, where the cost and difficulty of providing service is the greatest. In many areas, NTCA member companies are the only providers of video service to these customers.

NTCA members and other small video programming providers are adapting to the changing environment in the video marketplace by providing new ways to transmit video programming services to the consumer. Small video providers, however, face many obstacles when trying to obtain video programming from content providers and attempting to enter new markets. Unreasonable rates, exclusive dealing arrangements, abuse of market power through non-disclosure agreements, tying practices, predatory pricing, shared head-end reservations, and prohibitions on Internet protocol (IP) and analog transport are some of the barriers faced by small video providers. These and other barriers described below limit the full utilization of small carriers' broadband facilities.

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[2] 213 NTCA members provide cable television (CATV) service, 89 members provide direct broadcast satellite (DBS) service, and 465 members provide digital subscriber line (DSL) service. 2005-2006 NTCA Member Directory.

[3] NTCA recently released the results of its 2005 Broadband/Internet Availability Survey. Forty-two percent of those who responded to the survey offer video service to their customers. Ninety-four percent of those offering video do so under a cable franchise, while 6% offer video as an Open Video System, pursuant to Part 76, Subpart S of the Telecommunications Act of 1996. Fifty percent are utilizing hybrid fiber coax to offer video service, and 46% DSL. Of those respondents not currently offering video, 26% (14% of all survey respondents) plan to do so by year-end 2005. Seventy-eight percent of survey respondents expect to be offering video service by year end 2007. The full text of the NTCA 2005 Broadband/Internet Availability Survey Report is available on NTCA's Web site www.ntca.org.

Section 706 permits the Commission to consider appropriate regulating methods to remove barriers to investing in advanced telecommunications capabilities. Removal of these barriers will further the goals of Section 706 and enhance competition in the video marketplace. The Commission should recognize obstacles and adopt remedies where possible that will allow small video providers to gain access to video programming at reasonable rates. The Commission should also recommend in its report to Congress that Congress closely examine current laws and eliminate loopholes that allow for predatory pricing, anti-competitive behavior, and abuse of market power in the video services marketplace.

II SMALL MVPDS SERVING RURAL AMERICA FACE DIFFICULTIES GAINING ACCESS TO AFFORDABLE PROGRAMMING

The Commission asks a variety of questions about how video programming distributors package and market their programming. NTCA's members have much to say on this issue. The most commonly cited difficulties faced by carriers providing video in rural areas are the practices and charges of program distributors. In order to provide a video service, carriers must rely on program distributors for content. However, there is an unequal bargaining relationship which leads to some distributors charging outrageous prices and demanding unreasonable contractual terms.

A. Small Providers Lack Leverage in Their Negotiations with Video Content Providers

Access to video content at a reasonable price is essential for small providers of video service. NTCA's members who provide video service stated most often that about 50% of their operating expenses go to acquiring programming and that percentage is likely to increase. Contracts for programming typically contain automatic escalation clauses – forcing prices up by a certain percentage yearly. Small video service providers lack the leverage necessary to negotiate a better rate from the video programmers, forcing consumers in rural America to pay a premium for video service.

According to the National Cable Television Association (NCTA), nearly 103 million homes in the U.S. are passed by a local cable system.[4] The vast majority of these are passed by large multiple system operators (MSOs). However, many residents living and working in rural America receive their video service from small, rural providers.

Small video providers serving rural America lack the leverage of larger MSOs in dealing with content providers, to the detriment of rural consumers. In general, the larger the number of subscribers, the greater the degree of negotiating power and the better the eventual deal. Providers of programming content make much of their money by selling advertising, and can charge higher rates if they deliver more potential viewers. It is in the program providers' best interests, then, to take whatever steps are necessary to insure that their programming is carried by the larger MSOs. Content providers simply cannot afford to have the large MSOs not carry their content. The large MSOs use this fact to their own advantage. Consequently, they demand—and receive—more beneficial terms from the content providers than they otherwise might.

Smaller carriers, on the other hand, lack the leverage afforded by a large customer base, but their subscribers expect access to the same programming. Content providers are aware of this, and are thus able to take a relatively inflexible position in their negotiations with small carriers. Small carriers are not in a position to walk away from the negotiating table, and even if they did, the content providers' bottom line would be largely unaffected. Ultimately, this lack of leverage and negotiating power may lead to higher programming rates for the consumers served by smaller rural carriers.

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[4] NCTA, 2004 Mid-Year Industry Overview, p. 25. Available online at www.ncta.com/pdf_files/Overview.pdf.

Virtually all of the contracts negotiated between content providers and large MSOs include non-disclosure agreements. By restricting the flow of information, the content providers make it virtually impossible to establish any semblance of "market rates." Consequently, smaller carriers must enter into their negotiations at a significant disadvantage, as they possess far less information than the party with whom they are negotiating.[5]

B. Large Programming Distributors Demand Expensive and Unreasonable Contractual Terms

Without disclosing any specific contractual terms, NTCA member video providers complained of a wide range of practices that drive up the price of video programming.

Tying arrangements—whereby a network requires a carrier to take additional networks, as many as 12, in order to have access to a flagship network—are rampant. The end result is that the small carrier must pay a higher price in order to insure access to the desired flagship network. This problem is much more dramatic for a small carrier with limited capital resources than for a large MSO who can afford to pay for the extra networks.

In addition to forcing the rural MVPDs to provide programming their subscribers do not want or need, the program distributor may require that a large percentage of the subscribers receive the programming in order for it to be made available. Or, if the distributor makes the programming available no matter the number of subscribers, the price for programming increases if a certain percentage of households do not receive the programming. For example, a contract may provide that the price per subscriber for Sports Channel Y is $x if 85% of households receive the channel, but is (much higher rate) $z if less than that. In effect, the distributor of program Sports Channel Y ensures that the programming is carried on the lowest tiered offering

[5] This imbalance – dubbed by economists as "asymmetric information" – is a significant impediment to the establishment of an efficient marketplace.

of the rural video provider to reach all subscribers. In addition, contractual terms often dictate the channel on which the programming is to be provided.

These contractual terms are especially troubling in rural areas. In some rural communities there is no over-the-air reception of broadcast channels. Some rural consumers have no choice but to subscribe to a pay service to receive local television news, sports and entertainment. The price of service increases as more and more channels become part of the lowest priced, basic tier of video service. Some rural MVPDs complain that they have no option other than to provide all channels to all subscribers to meet the contractual penetration rates. There is no low-priced basic tier of service. Further, smaller carriers typically lack channel capacity, and these arrangements often compel smaller carriers to reposition (or even drop) channels in order to accommodate the additional networks forced on them by the flagship network. This repositioning and dropping of networks in a carrier's channel line-up combined with the expensive lowest tier offering causes consumer confusion and dissatisfaction and puts smaller carriers at a significant competitive disadvantage.

C. Small Carrier Access to Reasonable Program Rates According to Reasonable Terms is Essential to Ensure Rural Customers' Access to the Same Programming as Urban Customers

It is important that carriers in rural areas are able to obtain programming content at reasonable rates in order to be able to provide the same service to rural customers as is available in urban markets or in those served by large MSOs. Unless these rural carriers are able to gain access to the programming content that their customers deserve at reasonable rates, their customers will receive higher cost service than their urban counterparts. There is no justifiable reason that certain customers should be penalized for no other reason than that their service provider has fewer customers than a large MSO. Allowing small carriers equal access to programming choices at equivalent prices would go a long way toward insuring equivalent video services in urban and rural America, and between small and large providers.

III. NEW ENTRANTS INTO THE VIDEO MARKETPLACE

New entrants into the video marketplace face especially difficult challenges as they seek to compete. They are often entering into a market with new technology seeking to compete with an established provider. Experience has demonstrated that large, incumbent cable operators will engage in questionable practices in an effort to drive out competition.

A. New MVPDs Seeking to Serve an Area Served by an Established Large Cable Operator may Face Predatory Pricing Practices

The most onerous, and often times insurmountable, challenge for new entrants seeking to deliver video service is competing with the predatory pricing practices of large, incumbent cable operators. NTCA members who are using new technology to compete with large cable operators tell of troubling circumstances. More than one member explains that when they enter a market, the cable operator will drop its price for service way below cost in the areas where it faces competition – thus making it impossible for the new entrant to gain a foothold. The incumbent cable operator is able to afford this practice because it will increase the price for service in areas where there are no competitors. One NTCA member told of a cable operator who faced competition offering the deal of a lifetime to any subscriber who had switched to the competitor - a check for $300 and a contract offering the same service as was received from the competitor for a mere $5.00 a month for a number of years.

In the long run consumers do not benefit from win-back schemes of this kind. The cable operator is using profits from non-competitive markets to subsidize below-cost prices. The incumbent does not offer these prices to everyone, but only to subscribers who have already gone to a competitor or are in the process of doing so. The below cost prices are made available or extended in an attempt to drive the competitor out of the market. In the end, there is no effective competition.[6]

B. Existing Law and Regulation Contribute to Predatory Behavior

The Cable Television Consumer Protection and Competition Act of 1992 included a uniform rate requirement to prevent cable operators from having different rate structures in different parts of one cable franchise and to prevent cable operators from dropping the rates in one portion of a franchise area to under cut a competitor temporarily.[7]

In the Telecommunications Act of 1996, however, Congress amended the uniform rate requirement to add an "effective competition" exception.[8] An incumbent cable operator need not comply with the uniform rate requirement if it is subject to "effective competition." It is thus allowed to charge different prices to different segments of subscribers. The effective competition exception has been interpreted in a way that permits incumbent cable operators to engage in unfair practices. Local exchange carriers, by their entry into a video market may be the triggering event for the "effective competition" exception. [9] The FCC has found that "effective competition" can be found to exist as long as the LEC is planning to provide cable TV

[6] Congress was made aware of this and other anticompetitive practices of the MSOs in 2004. *See*, Testimony of the National Association of Telecommunications Officer and Advisors, United States Senate Committee on the Judiciary, *Cable Competition – Increasing Price: Increasing Value?* (Feb. 11, 2004). In addition to anticompetitive pricing behavior, the Association discussed problematic behavior of MSOs including: 1) Refusing to deal with suppliers and contractors that provide services to competitors; 2) Hiring away key employees of competitors; 3) Using litigation to prevent or delay competition; 4) Refusing to carry advertising of overbuilders; 5) Interfering with local franchise processes; 5) Flooding local media with misinformation about public communications initiatives; and 6) Lobbying for anticompetitive state laws.
[7] 47 U.S.C. Sec. 521(d). Normally, such practices would also violate the Sherman Act and/or Section 5 of the Federal Trade Commission Act. *See*, 15 U.S.C. Sec. 2 and 15 U.S.C. Sec. 45(a)(2).
[8] 47 U.S.C. Sec.543(d)
[9] 47 C.F.R. Sec.76.905(b)(4).

service in an area overlapping the incumbent's territory.[10] Under the FCC's interpretation of the LEC test, "effective competition" can be found even where the competitor has a minimal number of subscribers and where the vast majority of customers in a given area have no competitive alternative at all. Effective video competition will not be realized until this legal loophole is closed, preventing large, incumbent cable providers from engaging in practices intended to drive all competition from the market.

C. Incumbent Cable Operators May Abuse Their Market Power to Minimize the Programming Available to New Entrants

Some incumbent cable operators are using their market power to make it difficult for competitors to obtain programming. The incumbents know that without access to certain programming, competitors cannot make their service attractive to subscribers. Certain large cable incumbents are known to have entered into exclusive programming arrangements. Contracts are written in such a way as to bar new entrants access to local or regional sports or news programming. Local subscribers expect the programming and are unlikely to switch to a new provider who is unable to provide it.

Further, the association currently primarily responsible for negotiating programming for smaller video providers makes it difficult for new Telco-TV/IP-TV entrants to take advantage of the master affiliation agreements with programming distributors it negotiates on behalf of its members. In order to join, the company must be "engaged in the business of providing television reception or service to the public, *primarily by means of a cable television* system." The fee to join is reportedly $25,000 more for video providers without "significant cable experience" than for incumbent cable operators, no matter the technology actually employed for delivering the

[10] *See*, Commission Implements Cable Reform Rule Modifications: Provides Information of Cable Rate Regulation, CS Docket No. 96-85 (March 29, 1999). "Potential as well as actual LEC service can be considered [to determine whether a cable operator is subject to effective competition]"

programming. It appears to be another blatant example of incumbent cable operators protecting their businesses by driving up the cost of operation for new video competitors.

D. The IP-Transport Issue

New small Telco-TV/IP-TV providers are facing discriminatory practices concerning their ability to get into the video services marketplace and gain access to video content. For example, some video content providers prohibit their video content from being distributed through the use of DSL or the Internet. They claim that this IP-transport prohibition is required to prevent the piracy of their video content on the Internet. This concern, however, is easily addressed through today's encoding and encryption capabilities that enable IP-transport to be more secure than traditional cable transport. NTCA is concerned that some content providers/MVDPs/MSOs are using the false piracy excuse to actively discriminate against new Telco-TV/IP-TV entrants that are attempting to offer competitive video services in service territories currently served by existing MVDPs and MSOs. Such discriminatory practices should not be condoned by the Commission or Congress.

IV. THE SHARED HEAD-END ISSUE

Today, many small rural video providers would not be able to offer video services if they could not jointly purchase/lease a shared head-end with other small video providers. Some small video providers serve less than 300 residents within their service areas. If many small rural video providers were required to invest approximately $2-3 million in a head-end, manage and maintain the network, and absorb the programming costs, they could never expect to recover their investment nor provide affordable/competitive video services throughout their service areas. These same small video companies, however, have created an opportunity to provide video services by pooling their resources and jointly purchasing a head-end or leasing a head-end from another head-end owner. Sharing a head-end with several small companies substantially reduces initial investment and provides small video providers the opportunity to provide consumers with an affordable video services offering. Without the shared head-end option, many rural consumers would not have video service or would be limited to direct broadcast satellite service (DBS) without any other competitive offering.

Some video content providers are now taking issue with small providers sharing head-ends. Some content providers assert they are concerned with the ability of third parties (i.e., the controlling head-end entity) to manage administrative procedures for control of their content. For an example, they seek direct control of programming access for sporting event "black out" situations that may impact operators sharing a single head-end differently. In addition, if one operator from a shared head-end situation is not in good account standing, they seek the ability to cut off programming to that entity directly, and not through a third party (i.e. the head-end controlling entity).

Shared head-end video providers are concerned that when their current licensing agreements expire that they may be denied access to video programming from some content providers. Shared head-end providers are currently in negotiations with many content providers to resolve these issues so that consumers will receive uninterrupted video programming after their current licensing agreements expire. The Commission and Congress, however, should be aware of the shared head-end issue. If this issue is not resolved through negotiations prior to the expiration of many licensing agreements, many rural consumers may not have future access to existing video programming in their communities.

V. THE ANALOG TRANSPORT ISSUE

Traditional small analog CATV providers are also facing discriminatory practices concerning their future ability to offer video services using traditional analog cable networks. Some content providers are insisting that small analog cable TV providers upgrade their systems to a digital format for the transport of their video content. As described above, many small rural video providers do not have the economies of scale and scope to incur the cost of upgrading their analog networks to digital networks. For example, one NTCA member company provides video services using analog CATV to a community of 50 subscribers. If this company were to upgrade to a digital network today, it would be required to incur an expenditure of $180,000 - $250,000. This would result in such a substantial increase in rates to consumers that it would effectively put the small company out of the video business and leave the residents of the community with only one other option for video services – DBS. Such discriminatory practices should not be allowed.

VI. CONCLUSION

Unreasonable rates, exclusive dealing arrangements, abuse of market power through non-disclosure agreements, tying practices, predatory pricing, shared head-end reservations, and prohibitions on Internet protocol (IP) and analog transport are some of barriers faced by small video providers. Removal of these barriers will further the goals of Section 706 and enhance competition in the video marketplace. The Commission should recognize these obstacles and adopt remedies where possible that will allow small video providers to gain access to video programming at reasonable rates. The Commission should also recommend in its report to

Congress that Congress eliminate loopholes in the laws that allow for predatory pricing, anti-competitive behavior, and abuse of market power in the video services marketplace.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Gail Malloy, certify that a copy of the foregoing Comments of the National Telecommunications Cooperative Association in MB Docket No. 05-255, FCC 05-155 was served on this 19th day of September 2005 by electronic mail to the following persons.

/s/ Gail Malloy
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